



R/W MANUAL CHANGE

RWMC- 187



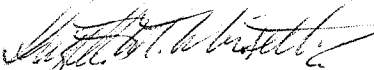
PROCEDURAL HANDBOOK
(1984 Edition)

RWPH-____-____-____
TRANSMITTAL#____

TITLE:

APPRAISALS

APPROVED BY:



SUZETTE M. MUSETTI

DATE ISSUED:

JAN 23 2009

Page 1 of 1

SUBJECT AREA:

CHAPTER 7 - APPRAISALS

ISSUING UNIT:

OFFICE OF APPRAISALS AND LOCAL PROGRAMS

SUMMARY OF CHANGES: Revises Section 7.17.00.00, Business Goodwill Appraisals, and updates its Table of Contents.

PURPOSE/PROCEDURES

This manual change:

- revises 7.17.06.00 to provide the District the option of preparing a memorandum appraisal for goodwill appraisals under limited circumstances.
- updates 7.17.16.00 by converting Metric units to English units.

Formatting update was applied and, where applicable, general typographical errors were corrected.

EFFECTIVE DATE

Immediately.

MANUAL IMPACT

- Remove the superseded pages and insert the attached pages in the Manual.
- Record the action on the Revision Record.

REVISION SUMMARY

Chapter

Remove Old Pages

Insert New/Revised Pages

Remove the following in its entirety:

Replace with the following in its entirety:

7 - Sections

Table of Contents (REV 12/2006)
7.17.00.00 (Rev. 3/2001)

Table of Contents (REV 1/2009)
7.17.00.00 (REV 1/2009)

CHAPTER 7

APPRAISALS TABLE OF CONTENTS

7.01.00.00	APPRAISAL POLICIES AND GENERAL REQUIREMENTS
01.00	General Overview
01.01	Definition of Market Value
01.02	Necessity for Appraisal
02.00	Appraisal Report Not Required
03.00	Uniform Relocation Assistance and Acquisition Policies Acts
04.00	Standards
05.00	Separation of Appraisal and Acquisition Functions
06.00	Prerequisites for " <i>Preliminary Right of Way</i> "
07.00	Dual Appraisal Requirements
07.01	Waiver of Dual Appraisal
08.00	Donations
08.01	Credit Toward State's Matching Share
09.00	Dedications
10.00	Notice of Decision to Appraise
11.00	Parcel Diary
12.00	Responsibility for Providing RAP Information
13.00	Legal Opinions
14.00	Responsibility for Preparation
15.00	Appraisal Review
15.01	Cumulative Review Concept
15.02	Review Appraiser Concept
16.00	Review Appraiser Process
16.01	Minor Deficiencies
16.02	Major Deficiencies
17.00	Approval Authority
18.00	Criteria for Use of Independent Fee Appraisers
19.00	Report Processing and Records
20.00	Letter of Transmittal
21.00	Tables
7.02.00.00	APPRAISAL REPORTS
01.00	Federal Project Numbers
02.00	Report Identification Numbers
03.00	Organization, Content and Sequence
04.00	Parcel Numbering
05.00	Number of Parcels Per Report
06.00	Parcels Straddling an Expenditure Authorization
07.00	Parcel Groups - Mutual Owners
08.00	Parcel Groups - Integrated Operation
09.00	Dual Appraisal Process
09.01	Corrections and Revisions
09.02	Review Process

7.02.00.00	APPRAISAL REPORTS (Continued)
10.00	Replacement Housing Valuation Reports
11.00	Calculations
12.00	Noncomplex Valuations of \$10,000 or Less
13.00	Waiver Valuation In Lieu of an Appraisal
13.01	Waiver Valuation (\$2,500 or Less) - Contents and Requirements
13.02	Waiver Valuation (\$2,501 to \$10,000) - Contents and Requirements
14.00	Nominal Values (\$2,500 or Less)
 7.03.00.00	 APPRAISAL PREPARATION
01.00	The Appraisal Page—Purpose
02.00	Appraisal Page Format
03.00	Alternate Appraisals
04.00	Appraisals of Excess Property for Acquisition
04.01	Uneconomic Remnants
04.02	Excess Acquisitions
04.03	To Avoid Large Windfall Relocation Payments to Single Family Owner-Occupants
05.00	Legal Larger Parcel and Subparcels
06.00	Allocation Between Excess and Right of Way
07.00	Excess Parcel Inventory Value (VTA)
08.00	Rental Rates
 7.04.00.00	 VALUE CONCEPTS AND CONSIDERATIONS
01.00	Value Basis
02.00	Total Value
03.00	Encumbered Fee
04.00	Mineral, Water, Oil and Gas Rights
05.00	Improvement Bonds and Assessments
06.00	Leasehold Interests “Bonus Values”
07.00	Waivers
08.00	Access Rights
09.00	Temporary Easements
10.00	Permanent Easements
11.00	Unit Values
12.00	Hazardous Waste and Hazardous Material Definition
12.01	Hazardous Waste General
12.02	Certification
12.03	R/W HW/Materials Coordinators Activities
12.04	Hazardous Materials
12.05	HW Site Identification
12.06	Notification
12.07	Valuation
13.00	Market Value of Nonprofit, Special Use Properties

7.05.00.00	METHODS OF VALUATION
01.00	Value Approaches
02.00	Sales Comparison Approach
02.01	Comparable Data
02.02	Analysis of Comparable Data
03.00	Assessor's Office Data
04.00	Cost Approach
05.00	Income Approach
05.01	Income Schedule
06.00	Review of Owner's Claimed Out-of-Pocket Expenses
7.06.00.00	LAND
01.00	General
02.00	Timber Land
03.00	Agricultural Land
04.00	Valuation of Open Space Land (Williamson Act, Timberland Production Zone, Farmland Security Zone, etc.)
05.00	Outdoor Advertising Sites
7.07.00.00	IMPROVEMENTS
01.00	General
02.00	Single Family Residence and Two to Four Unit Multi-Residence - Form Appraisal
03.00	Miscellaneous Improvements and Landscaping
04.00	Agricultural Improvements
05.00	Valuation of Fences
06.00	Valuation of Water Sources
07.00	Improvements - Little or No Value
08.00	Improvements - Interim Value
09.00	Improvements - Purchase or Curative Work?
10.00	Improvement Relocations or Replacements Exceeding Depreciated Value Less Salvage
11.00	Relocation, Rearrangement, or Reconstruction Estimates
12.00	Building Check Sheets
13.00	Service Station, Commercial and Industrial Buildings
14.00	Tenant or Lessee-Owned Improvements (Excluding Personal Property)
15.00	Retention Value
7.08.00.00	ITEMS PERTAINING TO THE REALTY
01.00	General
02.00	Appraisal Page Format
03.00	Replacement Cost
04.00	Depreciated Value
05.00	Salvage Value
06.00	Items Not Pertaining to Realty Under Section 1263.205

7.09.00.00 DAMAGES, BENEFITS, CONTRACT WORK

- 01.00 General
- 02.00 Severance Damages
- 03.00 Noncompensable Damages
- 04.00 Cost to Cure
- 05.00 Benefits
- 06.00 Summary of Severance Damages and Benefits
- 07.00 Damage Alternatives
- 08.00 Utility Service Damage
- 09.00 Construction Contract Work
- 10.00 Utility Main Relocations
- 10.01 Private Utility Connections
- 11.00 Access Openings

7.10.00.00 REVISION AND REVIEWS

- 01.00 General
- 02.00 Changes in Unapproved Appraisals Requiring Division Approval
- 03.00 Changes in Approved Appraisals-Unacquired Parcels
- 04.00 Revised Appraisal Pages
- 04.01 Submittal of Revised Pages
- 05.00 Revised Parcel Appraisals
- 06.00 Memorandum of Adjustment
- 07.00 Changes in Approved Appraisals on Acquired Parcels
- 08.00 Parcel Splits and Mergers
- 09.00 Parcel Cancellations
- 10.00 Review of Condemnation Parcels
- 11.00 Report Analysis for Nondelegated Parcels

7.11.00.00 OUTDOOR ADVERTISING SIGNS

- 01.00 Valuation
- 02.00 Definitions
- 03.00 Process
- 04.00 Payment Schedules/Application Renewal Permit Fees
- 05.00 Appraisal Procedures for Outdoor Advertising Signs

7.12.00.00 MOBILE HOMES

- 01.00 Mobile Homes - General
- 02.00 Mobile Homes - Realty
- 03.00 Mobile Homes - Personalty
- 04.00 Mobile Homes - Special Procedures
- 05.00 Mobile Homes - Format

7.13.00.00	SPECIAL APPRAISAL REPORTS
01.00	General
02.00	Material Site Appraisals
03.00	Disposal Site Appraisals
04.00	Office and Maintenance Station Site Appraisals
10.00	Joint Acquisition Appraisals
20.00	Protection Appraisals
30.00	Appraisals for Other Agencies
40.00	Staff Litigation Reports
 50.00	 UTILITY, RAILROAD AND GOVERNMENTAL OWNERSHIPS
50.01	Public Utility Property
50.02	Fee Land
50.03	Improvements
60.00	Railroad Property General Prerequisites
60.01	Valuation of Railroad Properties
70.00	Governmental, Indian, Functionally Replaced Publicly Owned Facilities, and State Land
 7.14.00.00	 EXCESS LAND APPRAISALS
01.00	General
01.01	Sale
01.02	Valuations
02.00	Review and Approval of Excess Land Appraisals and Public Sale Estimates
03.00	Public Sale Estimates
03.01	Format
03.02	Content
03.03	Examples of Supporting Data
04.00	Market-Value Appraisals - General
04.01	Market-Value Determination of \$10,000 or Less
04.02	The Appraisal Format, Content, and Standards
05.00	Review of Request for Proposal Submittals (RFP)
 7.15.00.00	 AIRSPACE ESTIMATES, BID LEASE VALUATIONS AND APPRAISALS
01.00	General
02.00	Estimates
03.00	Appraisals - General
03.01	Format
03.02	Standards and Methods
03.03	Preparation
04.00	Bid Lease Valuations
05.00	Rental Rate Appraisals

7.16.00.00 RENT DETERMINATION

- 01.00 General
- 02.00 Content
- 03.00 Review and Approval Process
- 04.00 Special Circumstances
- 05.00 Nominal Value Nonresidential Rentals

7.17.00.00 BUSINESS GOODWILL APPRAISALS

- 01.00 Statute - Compensation for Loss of Goodwill
- 02.00 Interpretation of the Eminent Domain Law, Court Cases, and Legal Issues
- 03.00 Burden of Proof
- 04.00 Notification Letter to the Business Owner
- 05.00 Timing for the Preparation and Completion of the Goodwill Appraisal
- 06.00 The Goodwill Appraisal Report
- 07.00 Parcel Diary
- 08.00 Cross-referencing the Goodwill and Real Estate Appraisal Reports
- 09.00 Parcel Numbering
- 10.00 Review and Approval Process
- 11.00 Project Influence
- 12.00 Appraisal Report Components and Sequence
- 13.00 Goodwill Valuation
- 14.00 Business Valuation Methods
- 15.00 Analyzing Financial Statements and State Income Tax Returns
- 16.00 Betterment at the Relocation Property
- 17.00 Disadvantages at the Relocation Property
- 18.00 Compensation to Business Owners Under the Relocation Assistance Program
(Pursuant to Section 7262 of the Government Code and 49 Code of Federal
Regulation Part 24)

7.17.00.00 - BUSINESS GOODWILL APPRAISALS

7.17.01.00 **Statute - Compensation for Loss of Goodwill**

Code of Civil Procedure, Title 7, Eminent Domain Law, Chapter 9, Article 6, Sections 1263.510, .520, and .530 provide the basis for compensating the owner of a business for the loss of goodwill. These sections should be reviewed by the appraiser prior to completing any appraisal involving a commercial property. See the reference volume.

7.17.02.00 **Interpretation of the Eminent Domain Law, Court Cases, and Legal Issues**

The courts are continuing to interpret the statutes on loss of goodwill. The first major court ruling by the State Supreme Court was the Department of Transportation v. Muller. This case has established that the increased cost of doing business at the replacement site is a compensable cost.

The Regions/Districts should consult with HQ R/W concerning any problems with interpretation of the compensability for loss of goodwill. Requests for legal opinions must be directed through HQ R/W for action by Sacramento Legal.

7.17.03.00 **Burden of Proof**

The law provides that a business owner shall be compensated for the loss of goodwill if the owner proves that the loss is caused by the State's taking of the property and that the loss cannot reasonably be prevented by a relocation of the business or by taking steps and adopting procedures that a reasonably prudent person would take and adopt to preserve the goodwill. The business owner has the burden of proof for loss of goodwill.

7.17.04.00 **Notification Letter to the Business Owner**

At the initiation of each staff real estate appraisal of a parcel occupied by one or more businesses, the appraiser will provide each business owner a written notification using Form RW 7-30 of the owner's rights to claim a loss of business goodwill. The notification letter will be sent to the business owner by certified mail, with return receipt requested. This form also includes a questionnaire asking for information about the business for the owner to return when claiming a loss of goodwill.

The letter will set a reasonable time limit for the owner to respond. No follow-up requests by the appraiser are required. The appraiser must not delay the initiation and completion of the real estate appraisal while waiting for the business owner to respond.

The date the notification letter is sent to the business owner and any responses from the owner, written or oral, must be documented in the parcel diary. The section of the parcel diary with entries relating to business goodwill shall subsequently be copied and attached to the parcel diary for the goodwill appraisal or a separate goodwill diary can be initiated.

If the owner does not submit a claim or makes a claim but does not furnish copies of State Income Tax returns, the appraiser must so document the parcel diary and the real estate report. The appraiser must still make a preliminary analysis and tentative conclusion as to whether or not the business owner will be able to relocate without a loss. The research and analysis for the tentative conclusion will be included in a separate section of the staff real estate appraisal or in the addendum to the report. The research and analysis will include, as a minimum, a statement of the observed availability of replacement sites.

7.17.05.00 **Timing for the Preparation and Completion of the Goodwill Appraisal**

It will be prepared as soon as possible after receiving the claim from the owner with copies of the owner's tax returns and any other supporting financial data that is furnished. To ensure confidentiality, only HQ R/W copy of the appraisal report will contain the owner's income tax returns. All goodwill appraisals will be in separate reports and not part of the real estate appraisal report.

The appraiser will not complete the goodwill valuation appraisal if the owner does not furnish copies of the State Income Tax returns. The appraiser will make a statement in the real estate appraisal report that since the owner has not furnished income tax returns, there is insufficient data to estimate whether or not the business possesses goodwill value in the before condition. Therefore, any loss of goodwill is indeterminable.

7.17.06.00 **The Goodwill Appraisal Report**

The Reports may contain more than one business goodwill parcel. They will be prepared by or under the direct supervision of, and the Report signed by, a Right of Way Agent of at least Associate Grade. The duties and responsibilities of the appraisers and reviewers are the same as those for real estate appraisals.

The appraisal will normally include a valuation in both the before and after condition in order to estimate the loss, if any. However, under certain circumstances it may not be necessary to value the business goodwill in either the before or after condition. This would be where the appraiser can clearly demonstrate, with support, that the business will not suffer a loss in the after condition.

One example would be a partial take of real property where the appraiser's analysis supports a conclusion that the taking and construction of the State's project does not affect the operation of the business in the after condition on the remainder. In other words, the State's taking and construction in the manner proposed does not diminish the business patronage or otherwise cause any reduction in net earnings. Another example would be where the appraiser determines that a business will not suffer any loss of goodwill at a new location because there will be no net loss of patronage and no increased costs of operation. These conclusions must be adequately supported and documented in the report.

Upon receipt of the goodwill questionnaire from the grantor, if the Senior Right of Way Agent determines it is obvious that there is no goodwill in the before condition (e.g., negative net income for the previous three years) as shown from the loss of business goodwill claim and tax returns for the previous five years, the Region/District has the option of utilizing a memorandum appraisal format or a very succinct narrative appraisal to document these conclusions. The memorandum is to give a full explanation of the valuation and will contain sufficient supporting documentation.

7.17.07.00 **Parcel Diary**

The appraiser will initiate a parcel diary, Form RW 7-23, for each goodwill parcel appraisal. A copy of the diary shall be included in the Report forwarded to HQ R/W.

7.17.08.00 **Cross-referencing the Goodwill and Real Estate Appraisal Reports**

The Report for the goodwill appraisal will carry the same basic number as the real estate Report with a subreference of the letter "G." For example, if the real estate Report is AR-7, the goodwill Report on a business located on the parcel will be numbered AR-7G1. Any subsequent reports made on other businesses located on properties appraised in AR-7 will carry AR numbers running consecutively, e.g., AR-7G2, AR-7G3, AR-7G4, etc.

A goodwill appraisal which supersedes a prior valuation of the same business will be given a new AR designation. The new Report will cross reference the prior appraisal(s). For example, "AR-7G8: This appraisal supersedes AR-7G3, approved (date)."

7.17.09.00 **Parcel Numbering**

The parcel numbers for goodwill parcels will be the same as the parcel number for the real estate on which the business is located with a subreference of G-1, G-2, G-3, etc., i.e., 12345 and 12345G-1.

7.17.10.00 **Review and Approval Process**

All noncondemnation goodwill appraisals will be reviewed for approval by the Division.

7.17.11.00 **Project Influence**

Goodwill valuations shall not include any increase or decrease in the value of the business that is attributable to the project. See Section 1263.330 of the Eminent Domain Law.

7.17.12.00 **Appraisal Report Components and Sequence**

- Appraisal Title Page - Business Goodwill Valuation - Form RW 7-24
- Parcel Summary Page - Goodwill - Form RW 7-25
- Business Goodwill Valuation - Senior Field Review Certificate - Form RW 7-26
- Business Goodwill Valuation - Certificate of Appraiser - Form RW 7-27
- Appraisal - Business Goodwill Valuation - Form RW 7-28
- Business Sales Data Page - Goodwill - Form RW 7-29
- Business Comparable Data Page - Goodwill - Form RW 7-31
- Purpose of Appraisal
- Date of Value

If the business has not relocated at the time of the appraisal, the date of value shall be the date of the appraisal, otherwise, the date of value shall be the date the business relocated.

- Description of Business

In addition to a comprehensive description of the business operation, include the name of business and the owner(s), location, history of the business ownership, areas of land and description of improvements used (owned or leased) by the business, lease/rental amounts and terms including expenses paid by tenant, geographical area served by the business, hazardous materials used by the business and hazardous waste observed.

- Recent sales of the subject business

Each sale of the subject business during the last five years preceding the appraisal will be explained in detail. Use a separate sales data page for each sale. The most recent sale during the period shall be verified by the appraiser with both seller and buyer, if possible. If not verified with both parties, efforts to do so must be described. A complete verification of the most recent sale will be made including sale price, terms, and a breakout of the amount paid for tangible and intangible assets such as machinery, equipment, liquor licenses, and goodwill. Any difference between the appraised value of goodwill and the price paid for goodwill must be explained.

- Availability of suitable sites for relocation

Include a detailed study of the availability or lack of availability of suitable replacement sites for the business. If the business has already relocated prior to the date of the appraisal, the analysis will state whether or not other suitable sites were available at the time of relocation and, if utilized, would have resulted in a lesser loss or no loss.

- Valuation

The valuation section shall include a comprehensive analysis of the appropriate approaches to value and the conclusion of the goodwill value at both the existing location and the new or proposed location. This also applies to businesses affected by partial acquisitions that may continue operations on the remainder.

- Reconciliation of valuation approaches and final conclusion

Where two or more approaches are used, the appraisal will reconcile the separate indications of value derived and include a reasonable explanation for the final conclusions of business goodwill. The final conclusion will state whether or not the business will suffer a loss of goodwill as a result of the taking. This will usually be a comparison of the goodwill valuation of the business at the old location and at the new or proposed location (before and after).

- List and valuation of tangible and intangible assets
- Comparable data pages and maps
- Index maps, subject map, relocation site map
- Parcel diary
- Addendum

The addendum should include supporting data such as financial statements, copies of income tax returns, relocation site studies, market analysis studies, questionnaire supplied by business owners, etc.

7.17.13.00 Goodwill Valuation

The first step is to estimate the value of goodwill, if any, of the business at the location being taken or affected by the project.

The premises for the goodwill appraisal should be consistent with the premises used in the real estate appraisal. Examples of premises that are ordinarily expected to be consistent are highest and best use, economic rent, value of business improvements such as fixtures, machinery and equipment. Any differences in these and other important elements must be explained in the Report.

Normally, the value of the goodwill is not estimated directly but by a residual process. The first step is to estimate the value of the total business enterprise and then subtract the value of the separately valued assets of the business, both tangible and marketable intangible, from the total value. The residual value, if any, represents the intangible asset of goodwill. The following is a summary of this residual process:

Total value of business	
(-) value of tangible assets owned by business	
(-) value of marketable intangible assets owned by the business	
Value of goodwill (intangible asset)	

(Intangible marketable assets are those which can be sold off separately from the business, such as a liquor license.)

If the analysis indicates no goodwill value, the process ends and the Report is completed. If no goodwill value exists in the before condition, there cannot be a loss of goodwill.

If the analysis results in a goodwill value, the appraiser must proceed with the appraisal process. The next step is to repeat the above process for the business as relocated, to determine the value of the goodwill at the new or proposed location. If the business has already relocated at the time of the appraisal, the business operation must be analyzed by repeating the valuation process outlined above to determine the value of the goodwill at the new location.

The compensable loss is the amount, if any, that the value in the before condition exceeds the value in the after condition.

Example:

Estimated value of goodwill before	\$15,000
Estimated value of goodwill after	<u>-10,000</u>
Estimated compensable loss of goodwill	<u>\$ 5,000</u>

If the business has not been relocated at the time of the appraisal, it will be part of the appraisal process to make a comprehensive study regarding the availability of either existing suitable sites or those sites that are expected to become available within a reasonable period of time to which the business can relocate. A suitable site is considered to be one which a prudent business owner would select in attempting to preserve goodwill to the greatest extent possible. The Report will contain a section detailing the appraiser's study of the availability or lack of availability of suitable replacement sites. If suitable sites are or will become available, the appraiser will value the goodwill in the after condition as described above as if the business were relocated to a property which would be selected by a prudent business owner seeking to preserve or enhance the value of the business goodwill. This is in keeping with the Eminent Domain Law (1263.510).

If the study shows that there are no available suitable sites, or none can be expected within a reasonable period of time, then whatever amount of goodwill value the business had before will be the loss of goodwill shown in the report. If these circumstances exist, the appraiser must fully document, in detail, the reasons why the business is unable to relocate.

If a business is highly complex or specialized it may be necessary or advisable to contract with consultants for appropriate market analyses and/or relocation studies.

7.17.14.00 **Business Valuation Methods**

There are many methods by which the value of a business and its goodwill can be estimated. The following are three methods commonly used for business valuation:

A. Market Approach

The most common market approach is the utilization of income multipliers derived from the market transactions of similar businesses. For example, retail store businesses might sell for two times annual gross income. Particular market multipliers may be based on income or sales and vary widely, depending on the type of business.

B. Capitalization of Excess Earnings

This is an income approach where excess earnings are calculated by subtracting from business net profit, a return on and of depreciable tangible assets and a return on marketable intangible assets. The return of a depreciable tangible asset is made over the remaining economic life of the asset. If marketable intangible assets have a limited life, then it will be necessary to also subtract a return of the asset over its remaining economic life. The excess earnings of a business, if any, are then capitalized at an appropriate rate to estimate the value of the goodwill.

C. Discounted Cash-Flow Analysis

This approach is focused on the projected earnings and expenses of a business over a period of time (usually the anticipated investment period). Value of goodwill is the present value of the projected net cash flow (either before or after taxes) for a period of years plus any reversion value of the goodwill. This method takes into account the effects of changes in the net return each year.

These are brief descriptions of the more commonly used valuation methods. For a more detailed explanation of the various valuation methods, the appraiser must refer to appraisal text books or other instructional manuals on business valuations.

7.17.15.00 **Analyzing Financial Statements and State Income Tax Returns**

In processing the various business valuation methods, such as the “capitalization of excess earnings,” it will be necessary to analyze financial statements and State income tax returns. As part of this process, the appraiser must reconstruct the income and expenses reported to arrive at a net income applicable to the value of goodwill.

The following list includes examples of items that must be considered in reconstructing the income and expenses reported:

- Depreciation must be deleted.
- Payments (principal and interest) on loans used to purchase the business must be deleted.
- Payments (principal and interest) on loans used to purchase real property must be deleted and an economic rent for the real estate used by the business substituted for the payment.
- Use economic rent instead of contract rent in the statement. Also, economic rent must be used at the new location. This approach is based on legal interpretation of the law. The appraiser must look at the real estate Report to see what was determined to be economic rent. An explanation must be made by the goodwill appraiser if the economic rent used in the goodwill appraisal is different than the economic rent used in the real estate appraisal. There could be a difference in the economic rents if substantial time elapsed between the date of the two appraisals.
- Owner's salary and draws must be adjusted to reflect reasonable compensation for the owner's role or activity in the business operation. In some cases, corporation officers receive a salary even if they do not work in the business. These salaries may be disguised as profit-sharing compensation and must be deleted because they are not an expense.

7.17.16.00 **Betterment at the Relocation Property**

In the process of reconstructing and/or estimating an income and expense statement for the business at a relocated property, the appraiser must adjust the statement for avoidable property betterments. The following is an example of an avoidable betterment which must be adjusted in the income and expense statement as a part of the process of estimating goodwill value at the new business location.

Assume that the business at the old location occupied a building containing 9,700 sq ft with an economic rent of \$10,000/month. Also assume that the business owner chose to relocate to a 15,000 sq ft building with an economic rent of \$15,000/month, even though there were other suitable relocation properties on the market containing 9,700 sq ft at a rent of \$10,000/month comparable to the old property. In this example, the appraiser must use an economic rent of \$10,000/month in the statement instead of the actual rent of \$15,000/month at the new location.

On the other hand, an adjustment should not be made if there were no other comparable replacement properties available in the market with 9,700 sq ft renting for \$10,000/month, and the owner was forced to relocate to a 15,000 sq ft, \$15,000/month rent in order to continue business and preserve the goodwill (patronage). This may be considered an "unavoidable betterment." In this case, the appraiser must use an economic rent of \$15,000/month. However, if the business owner were forced to relocate to the larger 15,000 sq ft building, but could sublet the 5,000 sq ft of excess area for \$5,000/month, then the appraiser must, of course, take that rental income into account at the new location.

The appraiser must be careful in deciding which betterments must be adjusted as part of the process of estimating the value of the goodwill at the relocated property in the after condition. The basis for the appraiser's decision that there is an "unavoidable betterment" must be included in the goodwill report. If the Region/District has any difficulty in identifying betterments which should be adjusted, HQ R/W Appraisal Branch should be consulted. There may be a need to request legal advice on specific issues.

7.17.17.00 **Disadvantages at the Relocation Property**

There may be certain conditions at the relocated property which cause a reduction of net income and, thus, a reduction from the level of goodwill value that the business had at the old location (loss of goodwill). Some examples are loss of net patronage and increased (economic) rent or other increased operating expenses. (The increased rent or other expenses must, of course, not be a result of avoidable betterments.)

Note that the words “loss of net patronage” are used in this section. The reason that the word “net” is used is because Eminent Domain Law Section 1263.510, paragraph (b), states “within the meaning of this article ‘goodwill’ consists of the benefits that accrue to a business as a result of its location, reputation for dependability, skill, or quality, and any other circumstances resulting in probable retention of old or acquisition of new patronage.” Therefore, if some of the old patronage were lost by the move, but an equal amount of new patronage was gained at the new location, there would be no net reduction of patronage.

If the Region/District has any difficulty with a particular appraisal in determining which disadvantages must be considered in estimating the compensable loss of goodwill, HQ R/W Appraisal Branch should be consulted. There may be a need to request legal advice on specific issues.

7.17.18.00 **Compensation to Business Owners Under the Relocation Assistance Program (Pursuant to Section 7262 of the Government Code and 49 Code of Federal Regulation Part 24)**

Certain compensable goodwill losses and Business Relocation Assistance Program items may fall into overlapping areas of the various laws. An owner is entitled to only one payment for a loss. Therefore, the appraiser must furnish the best information possible as to identifying the components of a loss of goodwill. It is then up to the Acquisition and RAP Branches to apply the information appropriately in determining proper payments. This will ensure compliance with 49 CFR 24.3 NO DUPLICATION OF PAYMENTS. The statute for compensation for loss of goodwill, Code of Civil Procedure Section 1253.510, provides that there shall be no duplication of payments for loss of goodwill which are provided to the business owner pursuant to the Relocation Assistance Program. In addition, Section 1263.010 of the CCP provides “where two or more statutes provide compensation for the same loss, the person entitled to compensation may be paid only once for the loss.”

The following are items for which the business owner may receive compensation under the Relocation Assistance Program. Some of these may also be included in a particular finding of a loss of goodwill. The Relocation Assistance Program covers the following:

- A. Actual reasonable moving and related expenses (49 CFR Part 24.303).
- B. Reestablishment expenses (limit \$10,000) (49 CFR Part 24.304). (Only “small businesses” are entitled to compensation for these reestablishment expenses. A small business is defined [49 CFR 24.2(t)] as a business having not more than 500 employees working at the site being acquired or displaced. Sites occupied solely by outdoor advertising signs, displays or devices do not qualify as a business for purposes of receiving reestablishment benefits under 49 CFR 24.304.)
 - 1. Eligible expenses. Reestablishment expenses must be reasonable and necessary, as determined by the State. They may include, but are not limited to, the following:
 - a. Repairs or improvements to the replacement real property as required by Federal, State, or local law, code, or ordinance.

- b. Modifications to the replacement property to accommodate the business operation or make replacement structures suitable for conducting the business.
 - c. Construction and installation costs, for exterior signing to advertise the business.
 - d. Provision of utilities from right of way to improvements on the replacement's site.
 - e. Redecoration or replacement of soiled or worn surfaces at the replacement site, such as paint, paneling, or carpeting.
 - f. Licenses, fees, and permits when not paid as part of moving expenses.
 - g. Feasibility surveys, soil testing, and marketing studies.
 - h. Advertisement of replacement location.
 - i. Professional services in connection with the purchase or lease of a replacement site.
 - j. Estimated increased costs of operation during the first 2 years at the replacement site for such items as:
 - (i) Lease or rental charges
 - (ii) Personal or real property taxes
 - (iii) Insurance premiums, and
 - (iv) Impact fees or one-time assessments for anticipated heavy utility usage.
 - k. Other items that the State considers essential to the reestablishment of the business.
- C. In Lieu Payment (not less than \$1,000 nor more than \$20,000) (49 CFR Part 24.306). (This is a payment in lieu of moving and related expenses, actual reasonable reestablishment expenses, and loss of patronage.)

A business owner may be entitled to payments for eligible items listed under both Categories A and B. As an option, a business owner may elect to receive a payment under Category C, "In Lieu Payment." If the owner selects the "In Lieu Payment," the owner is not entitled to any payments under either Categories A or B. It should be noted that the portion of the in-lieu payment that is not moving and related costs must be offset against goodwill.

To enable the Acquisition and RAP Agents to comply with the law and fully compensate the business owner for proper costs and/or losses, but still ensure there is no duplication of payment, the appraiser must show the following in any goodwill appraisal which finds a compensable loss of goodwill:

The appraiser must list in the Loss of Goodwill Appraisal Report each of the items listed above which contributed to the loss of goodwill, i.e., any of the eligible reestablishment expenses and/or loss of patronage which contributed to the loss of goodwill. The amount of loss of goodwill attributed to each such item shall be shown separately, if possible.

Example:

Total estimated loss of goodwill:	\$18,000
Allocation (causes of the loss):	
1. Increased economic rent	9,000
2. Necessary modification at new location	4,000
3. Loss of patronage	<u>5,000</u>
Total Loss	\$18,000

If the goodwill appraisal report concludes a loss of goodwill, the appraiser is to include a statement in the appraisal that if any amounts relating to loss of goodwill were paid to the business owner under the Relocation Assistance Program, such amounts must be deducted from the amount of the loss of goodwill shown in the appraisal report. The purpose of the statement is to serve as a reminder to the acquisition agent and to the Relocation Branch that no duplication payments for loss of goodwill are to be made as provided in the Eminent Domain Code.

See the Relocation Assistance Chapter for further information.